

Texas Economic Development Bank

Fiscal Year 2016 Annual Report

Reporting Period: September 1, 2015 to August 31, 2016



OFFICE OF THE GOVERNOR
ECONOMIC DEVELOPMENT & TOURISM

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Overview of Economic Development Bank Programs

The Texas Economic Development Bank (the Bank) operates within the Office of the Governor's (OOG) Texas Economic Development and Tourism Office (EDT). The Bank was created to oversee certain state economic development programs and to develop a comprehensive and coordinated approach to assist businesses and local communities. The Bank operates an economic development portfolio comprised of financial and business development programs to assist communities and businesses in developing and achieving economic success, as directed by *Government Code Section. 489.108*.

Sec. 489.108. PROGRAMS, SERVICES, AND FUNDS UNDER BANK'S DIRECTION.

Notwithstanding any other law, the bank shall perform the duties and functions of the office with respect to the following programs, services, and funds:

- (1) the capital access program established under Section 481.405;
- (2) the Texas leverage fund;
- (3) the enterprise zone program established under Chapter 2303;
- (4) the industrial revenue bond program;
- (5) the defense economic readjustment zone program established under Chapter 2310;
- (6) the Empowerment Zone and Enterprise Community grant program established under Section 481.025; and
- (7) the Renewal Community program.

The Empowerment Zone, Enterprise Community and the Renewal Community programs were federal programs that have expired and are therefore no longer a part of the Bank's program offerings.

The Bank provides numerous program options and related assistance through finance and tax incentive programs. The programs target three key audiences: Texas businesses; communities; and other public and private financing contributors. In addition to helping cultivate Texas' home-grown economy, the Bank also provides incentives to businesses wishing to relocate or expand in Texas.

The Bank's effectiveness is measured by the number of jobs created and retained and the total amount of non-state funds leveraged as a result of its efforts. The Bank was established for the statutory purposes of:

- Providing globally competitive, cost-effective state incentives to expanding businesses operating in this state and businesses relocating to this state; and
- Ensuring that communities and businesses in this state have access to capital for economic development purposes.

The Bank's public finance programs provide financing to communities and businesses so they may in turn create additional employment opportunities and foster economic diversity and vitality.

Public Finance Programs

- Product Development and Small Business Incubator Funds
- Industrial Revenue Bonds
- Texas Leverage Fund
- Capital Access Program

The Bank's tax incentive programs focus on job creation, retention, and capital investment in Texas.

Tax Incentive Programs

- Enterprise Zone Program
- Defense Economic Readjustment Zone

In Fiscal Year (FY) 2016, the Bank provided assistance through public finance and tax incentive programs that generated 1,640 new jobs, helped retain 17,060 jobs, and aided in the development of 81 new projects producing more than \$3.5 billion in capital investments for the state. In addition, the Bank's finance programs supported 34 new loans totaling \$1,556,894 and approved eight bond issuances totaling \$329,395,000.

Reporting Requirements

In 2003, the Texas Legislature authorized the Bank to administer the programs under *Government Code Section 489.108*. As part of that charge, the Bank is required to submit an annual status report to the Texas Legislature and the Legislative Budget Board. This report is submitted in fulfillment of the statutory requirement under *Government Code Sec. 489.107* which states that on or before January 1 of each year, the office shall submit to the legislature an annual status report on the activities of the Bank.

Product Development Fund and Small Business Incubator Fund

The Product Development Fund and Small Business Incubator Funds (collectively PDSBI), are revolving loan programs approved by the voters of the state in 1989 in a constitutional amendment (Article 16, Section 71) authorizing the issuance of \$25 million of bonds for Product Development and \$20 million of bonds for a Small Business incubator program. The program was established through the issuance of \$45 million of General Obligation (G.O.) bonds in FY 2005.

The purpose of the Product Development Fund is to provide financing to aid in the development, production, and commercialization of new or improved products in the state, while the Small Business Incubator Fund provides financing to foster and stimulate the development of small businesses. Per statute, in determining eligible projects and businesses, special preference is given to products or businesses in the areas of semiconductors, nanotechnology, biotechnology, and biomedicine that have the greatest likelihood of commercial success, job creation, and job retention in the state.

The programs are designed to be self-supporting with capital and administrative costs paid for by the loan participants' repayments. Any bond proceeds that have not been loaned to program participants are held and invested in the state's treasury.

Two new loans totaling \$730,000 were funded during FY 2016:

- A loan of \$180,000 was disbursed to help a company finance the expansion of its current facility and to purchase machinery. This financing will help the business retain at least 17 jobs.
- In FY 2016 a loan of \$550,000 was disbursed to PeopleFund, a non-profit micro-lending institution, to provide additional funding for the PeopleVET revolving loan program for veteran entrepreneurs and for educational training programs for veteran small business owners across the state. This \$550,000 loan is in addition to a \$500,000 PDSBI loan disbursed in FY 2015 to support the PeopleVET program. In FY 2016, the PDSBI Board approved a motion to forgive the original \$500,000 loan by accelerating the provisions of the loan and security agreement. As a condition for having the loan forgiven, all of the loans tied to the original \$500,000 loan had to be pledged as collateral for the FY 2016 \$550,000 loan. The combination of these two loans has allowed the PeopleVET program to support at least 27 veteran-owned businesses to date.

Industrial Revenue Bond Program

The Texas Industrial Revenue Bond Program (IRB) provides tax-exempt or taxable long-term financing for projects as defined in Chapter 501 of the Texas Local Government Code. The statute allows cities, counties, and conservation and reclamation districts to form non-profit Industrial Development Corporations (IDC) or authorities. Under Sec. 501.006., a local unit of government may use a corporation to issue bonds on the unit's behalf to finance the cost of a project, including a project in a federally designated empowerment zone or enterprise community or in an enterprise zone designated under Chapter 2303, Government Code, to promote and develop new and expanded business enterprises for the promotion and encouragement of employment and the public welfare.

An IDC issues tax-exempt and taxable bonds for eligible projects in its jurisdiction and acts as a conduit through which bond proceeds are channeled.

Generally, all debt service on the bonds is paid by the participating business under the terms of a lease, sale, or loan agreement. As such, it does not constitute a debt or obligation of the IDC, a governmental unit, or the State of Texas.

In FY 2016, the Bank received and approved seven IRB project applications totaling \$329,395,000. These projects collectively supported the creation of 224 new jobs, the retention of 927 jobs, and the expenditure of \$1,866,478,817 in capital investments. A map showing program activities by region is included in **Exhibit 1**. The table on the following page provides details on the seven approved bond projects.

APPROVED BOND PROJECTS FOR FY 2016

Community	Issuer	Business Name	Bond Amount	New Investments (Project Costs)	Project Description	New Jobs	Retained Jobs
Cass County	Cass County IDC	International Paper Company	\$4,560,000	\$4,560,000	Refinance the acquisition and construction of certain solid waste disposal, wastewater treatment, sewage, and/or pollution control facilities.	0	799 (including hourly)
Hartley County	Dallam County IDC	Morning Star Dairy, LLC	\$5,350,000	\$5,149,448	Financing solid waste disposal components of a heifer facility and a dairy facility.	24	0
City of San Antonio	City of San Antonio Industrial Development Authority	Tindall Corporation	\$8,600,000	\$8,740,000	Refinancing a manufacturing facility.	0	106
City of El Paso	Mission EDC	EWM P1, LLC	\$48,000,000	\$69,266,332	Finance or refinance costs for water treatment plant.	0	10
City of Conroe	Mission EDC	AmeriTex Pipe and Products, LLC	\$2,500,000	\$18,893,051	Refinance the acquisition and installation of equipment to manufacture concrete pipes, culverts and manhole products.	120	0
City of Conroe	Mission EDC	Concrete Real Estate Investment	\$7,500,000				
City of Beaumont (Jefferson County)	Mission EDC	Natgasoline LLC	\$50,000,000	\$1,759,869,986	Development of a methanol production facility – bond proceeds used to finance the portion related to the sewage facility components.	80	12
			\$202,885,000				
TOTALS			\$329,395,000	\$1,866,478,817		224	927

Texas Leverage Fund Program

Introduced in 1992, the Texas Leverage Fund (TLF) provides an additional source of financing to communities that have adopted the Texas Economic Development Sales Tax (Type A/Type B). The program allows communities to leverage future sales tax revenues to expand economic development through business expansions, business recruitment, and exports. The program was created pursuant to the provisions of Section 52-a of Article III of the Constitution of the State of Texas, Vernon's Texas Civil Statutes, Title 83, Article 5190.6, Development Corporation Act of 1979, Chapter 481 of the Texas Government Code (the "Act"), and Chapter 1371, of the Texas Government Code ("Chapter 1371").

Loan terms are available for either long-term or interim financing with maturities of up to 15 years. Other advantages of this program are that communities can quickly access required capital, and there is no penalty for pre-payment of loans.

Economic development sales tax revenues serve as collateral for loan repayment with required minimum debt service coverage ratios specified in the TLF Program guidelines.

Chapter 501 of the Local Government Code allows Type A & B development corporations to use loan proceeds to pay for allowable project costs relating to land, buildings, equipment, facilities, expenditures and improvements. Chapter 505 of the Local Government code further allows Type B development corporations to use loan proceeds for projects relating to recreational or community facilities, recycling facilities, affordable housing and certain other programs.

At the end of FY 2016, there were 22 loans outstanding with a combined balance of more than \$16 million. There were no new loans completed in FY 2016 and no loans paid in full.

Recommended Legislation for the TLF Program

During the 85th Legislative Session, the Office of the Governor will work closely with the Legislature to add legislation to authorize the OOG to continue operation of the existing Texas Leverage Fund commercial paper note program within the Bank. The recommended legislation will strengthen the statutory authority of the program to allow OOG staff to operate the program in the most efficient way possible under the guidance of the changes from the Legislature.

Capital Access Program

The Capital Access Program is designed to increase the availability of financial loans for businesses and nonprofit organizations that face barriers to accessing capital or fall outside the guidelines of conventional financing. Loans may only be used for working capital, which includes the purchase, construction, or lease of capital assets. Construction or purchase of residential housing and simple real estate investments (excluding those occupied by the applicant's business) are ineligible uses of capital access proceeds.

To be eligible, the borrower must be both: 1) a small or medium-sized business (499 employees or fewer) or a nonprofit organization; and 2) located in Texas or having at least 51 percent of its employees located in the state.

Participating lenders must set up reserve accounts to which contributions are made by the borrower, lender, and the State of Texas. All contributions from Capital Access Program loans are deposited into these reserve accounts, and in the event of a loan default, the lender can withdraw the defaulted amount and other fees to recoup any losses. The lender and borrower together must contribute, at minimum, 4 percent of the loan amount to the reserve fund. Additionally, the State of Texas must contribute 8 percent of the loan amount. The program presently has two participating lenders: 1) PeopleFund; and 2) LiftFund.

Since the program's re-launch in FY 2016, the Program has facilitated 32 loans for small businesses throughout the State, with an overall loan amount of \$826,894. Additionally, the program has facilitated \$826,894 dollars in capital investments, with the State contributing \$59,815 to the reserve fund in FY 2016. The program currently stands at a zero default rate. A map showing loan totals by region is included in **Exhibit 2**.

Texas Enterprise Zone Program

The Texas Enterprise Zone Program (TEZ) encourages local communities to partner with the State of Texas in job creation efforts and capital investment, particularly in economically distressed areas of the state.

Local communities must nominate a company as an Enterprise Project to be eligible to participate in the program. Legislation provides a maximum of 105 enterprise zone project designations per biennium. Local communities are limited by statute in the number of enterprise zone designations they may award.

Designated projects are eligible to apply for a refund of state sales and use taxes paid on expenditures at the qualified business site during the five-year designation period. The level and amount of refund are related to the capital investment and jobs created and/or retained at the qualified business site.

In FY 2016, the Bank approved 39 Enterprise Project applications, totaling 38.5 designations. One of the project applications requested and was approved for a half-designation. These 38.5 approved project designations, once completed, will result in an estimated capital investment of \$1.7 billion, 1,420 new jobs and 116,116 retained jobs. The Comptroller of Public Accounts reported \$24.06 million in state sales and use tax refunded during FY 2016. A map showing Enterprise Zone-supported jobs and capital investment by region is included in **Exhibit 3**.

Fiscal Year	Approved Projects	Project Designations	Capital Investments	New Jobs	Retained Jobs	Refund of Sales & Use Taxes
2016	38.5	38.5	\$1.7 billion	1,420	16,116	\$24.06 million

TEZ Reporting Requirements

The Bank is required to submit an annual evaluation report to the Texas Legislature and the Legislative Budget Board which evaluates the program's effectiveness, describes the use of state and local incentives and the effect on revenue, and suggests legislation as appropriate

(Government Code, Chapter 2303. Subchapter B, Section 2303.052). This report is submitted in fulfillment of the program's statutory requirements:

Sec. 2303.052. BANK REPORT REGARDING PROGRAM. The Bank must include the following information regarding the enterprise zone program in the report required by Section 489.107:

- (1) an evaluation of the effectiveness of the program;
- (2) a description of the use of state and local incentives under this chapter and their effect on revenue; and
- (3) suggestions for legislation with regard to the program.

Evaluation of Program Effectiveness

Fifty-one communities with active enterprise zone projects submitted annual reports to the office for FY 2016. When asked to evaluate how effective the program has been toward achieving the community's revitalization goals for the next five to ten years, 35 percent of the communities responded that it exceeded expectations; 61 percent responded that it was somewhat successful; and 6 percent responded that it was unsuccessful.

These communities also reported more than \$16 billion in combined projected capital investments and more than \$164 million in net new revenues (sales and property taxes, fees, etc.) as a result of economic development activities and incentives.

Use of State and Local Incentives and Effect on Revenue

TEZ is an active and popular economic development incentive tool for businesses looking to bring capital investment and jobs to a community. Although the law limits enterprise project allocations per biennium, Texas is experiencing an increased interest in the TEZ program. This is due, in large part, to the 78th Texas Legislature's decision to allow projects to be located outside of an enterprise zone area if the project draws at least 35 percent of its employees from enterprise zone residents or economically disadvantaged individuals, as defined by the act. About 48 percent of the designations awarded during FY 2016 were located outside of an enterprise zone area.

Each year, local enterprise zone administrators participate in a survey to determine the effectiveness of the program at the local level. TEZ administrators reported that, for FY 2016, participating communities received almost \$644 million in total revenue (related taxes and fees) due to active enterprise zone projects. Of this amount, communities granted back to Enterprise Zone Projects approximately \$130 million (19 percent of total revenue) for a net revenue collection of \$514 million.

Recommended Program Changes and Program Improvement Activities

The 84th Legislature passed SB 100, which became effective September 1, 2015. This bill changed numerous aspects of the TEZ program, as listed below:

- Introduction of "half designations," which allow smaller communities to use one half of an authorized designation for a project for a maximum of 250 jobs to be retained or

created for benefit with a maximum refund of \$125,000 each state fiscal year. The maximum rebate available for a half enterprise project is \$625,000.

- Requires that an inter-local agreement be executed between a county and a local municipality if the county wants to nominate a project inside of a local municipality within the county.
- Counts only new jobs for per worker tax refund incentives for “Double” and “Triple” Jumbo awards (i.e., larger projects with tax refunds in the range of \$1.25 million to \$3.75 million).
- Includes veterans as an option for the types of workers that may satisfy the new job hiring requirement.
- Limits the use of site designations so no more than two active designations may occur at the same qualified business site at one time.

These changes to the program will likely induce greater participation among eligible Texas communities, especially rural communities with the use of half projects, and will support the creation of new jobs in Texas. At this time staff, does not recommend any further changes.

Defense Economic Readjustment Zone

The Defense Economic Readjustment Zone Program was created in 1997 by the 75th Texas Legislature as a tool for business recruitment and job creation in adversely impacted military communities. It is designed to provide assistance to Texas communities, businesses, and workers impacted by, or vulnerable to, the closure or realignment of military installations and the reduction of federal defense contracting expenditures.

Since its inception, six zones and five project applications have been approved by the Bank. Zones are designated for a period of seven years while projects are designated for a period of five years from the date of approval.

Local communities must nominate a company as a Defense Economic Readjustment Zone Project in order to be eligible to participate in the program. Qualified businesses designated as DERZ projects are eligible for a state sales and use tax refund on expenditures of qualifying items. Under DERZ, the level and amount of the tax refund is related to the sales and use tax paid on expenditures of qualifying items and the number of jobs created/retained at the site.

Local communities participating in the program may offer benefits to participants under the DERZ program including but not limited to local property tax abatement, tax increment financing, one-stop permitting, and other incentives. The most common local incentives available in the DERZ communities are tax abatement, infrastructure improvements, and training programs.

In FY 2016, the DERZ program did not receive any applications and currently is not administering any active projects. Also, there are currently no active designations established for the DERZ program. The last zone designation in McGregor expired in September 2015.

Exhibits: Maps of Programs by Region

Exhibit 1

Industrial Revenue Bond Program

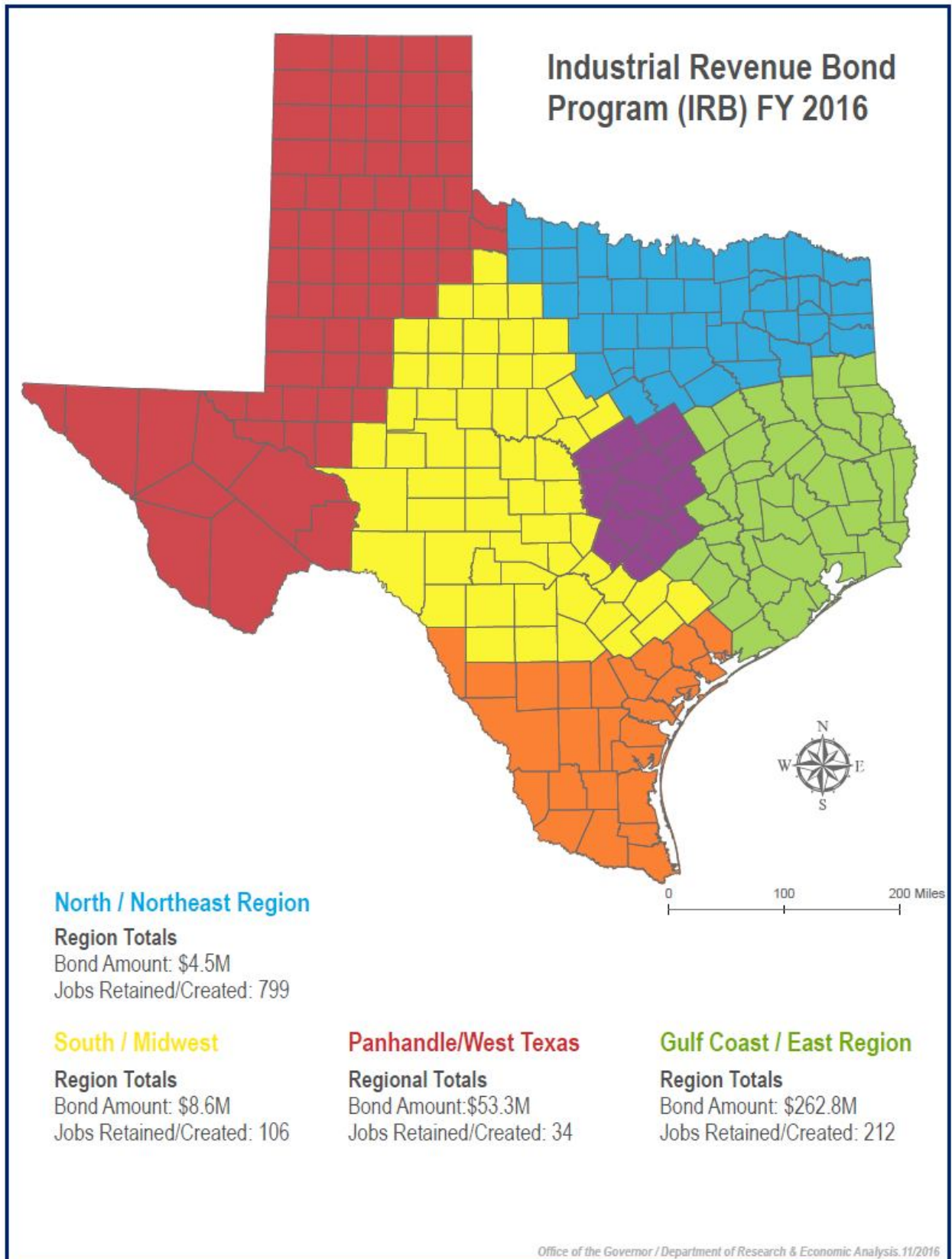
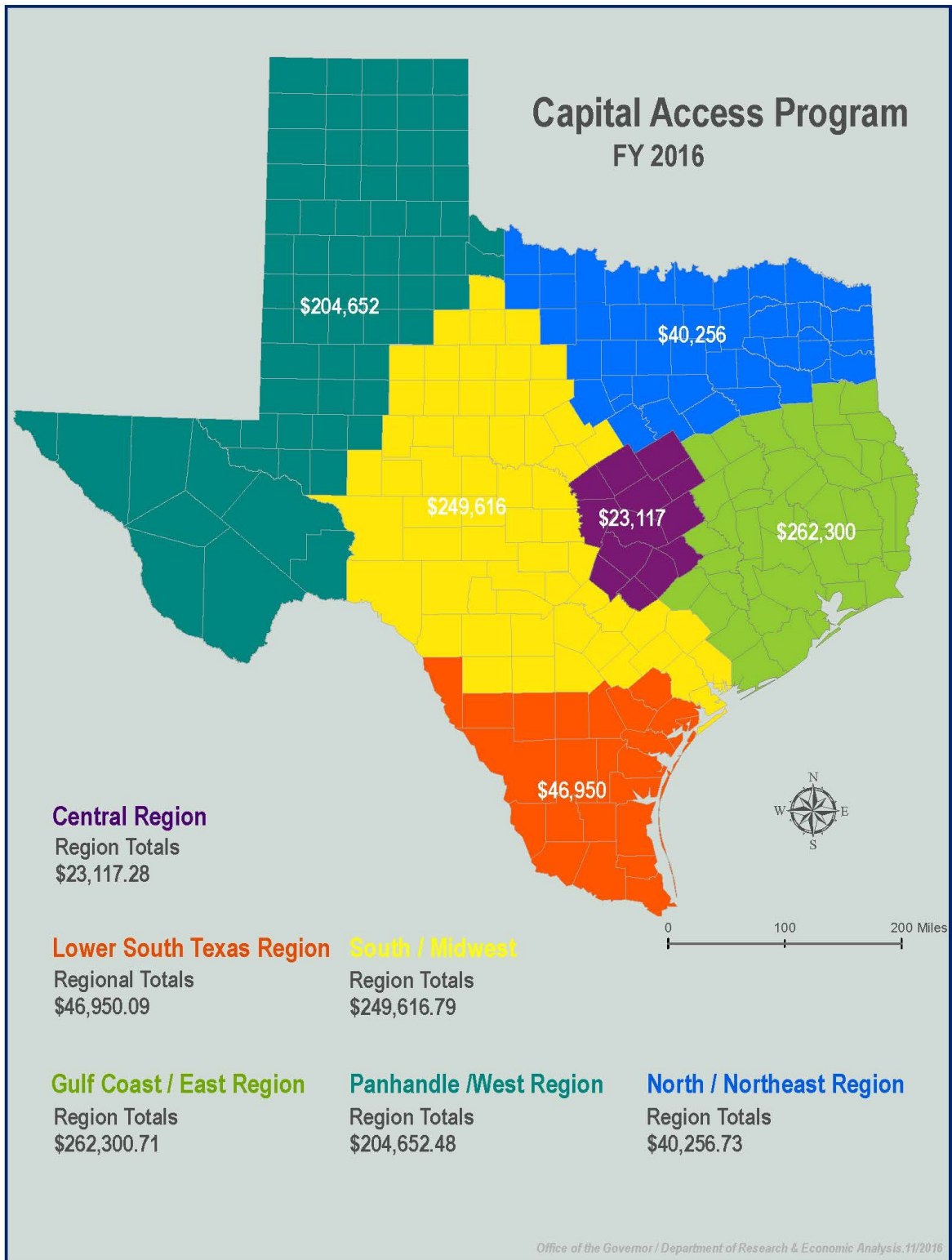
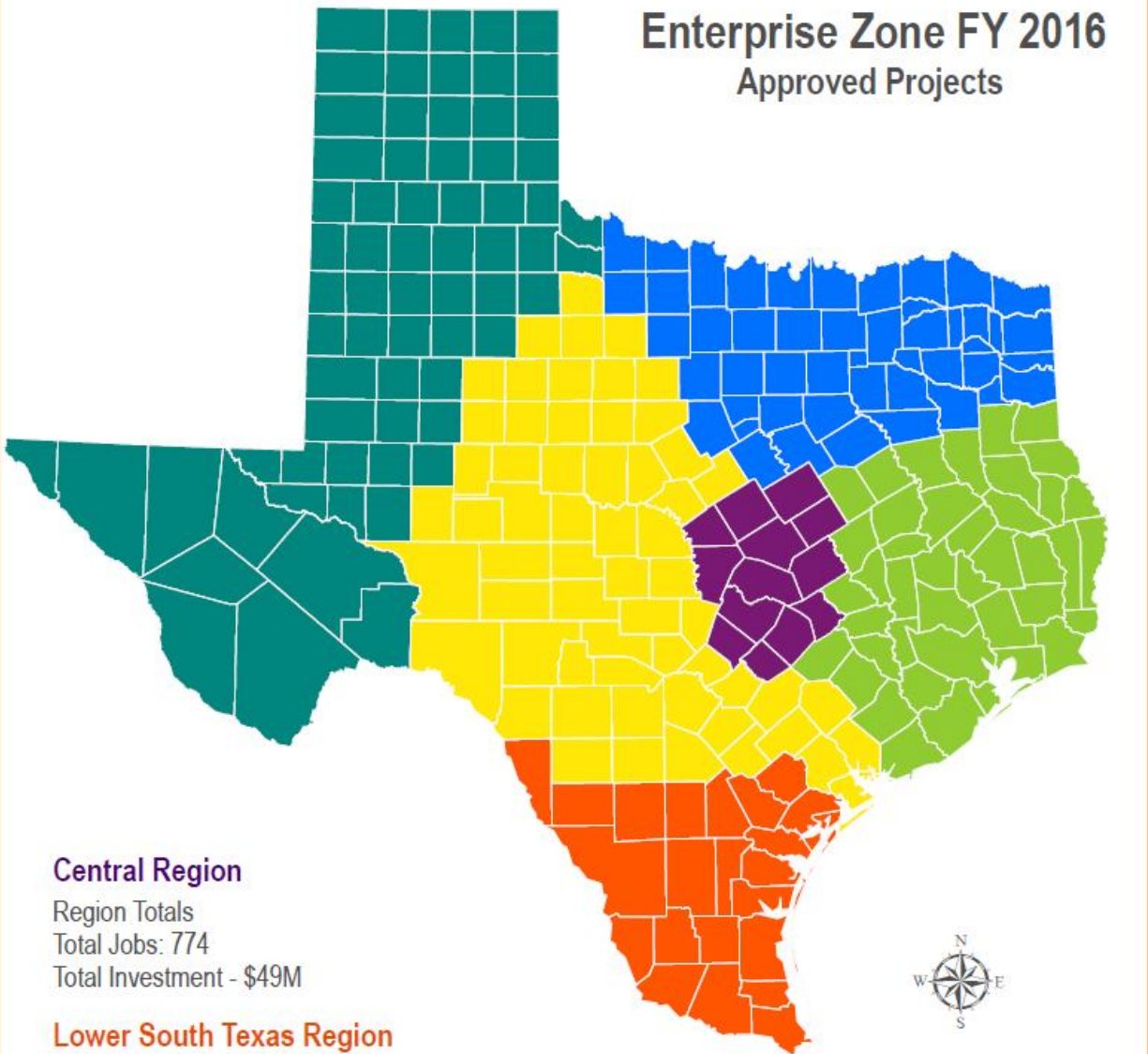


Exhibit 2

Capital Access Program



Enterprise Zone FY 2016 Approved Projects



Central Region

Region Totals
Total Jobs: 774
Total Investment - \$49M

Lower South Texas Region

Regional Totals
Total Jobs: 1,000
Total Investment: \$235M

Gulf Coast / East Region

Region Totals
Total Jobs: 4,749
Total Investment: \$827M

Panhandle / West Region

Region Totals
Total Jobs: 2,177
Total Investment: \$77M

North / Northeast Region

Region Totals
Total Jobs: 8,836
Total Investment: \$514M



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PO Box 12428, Austin, Texas 78711
512-936-0101
www.TexasWideOpenForBusiness.com